

Suits Say Unscrupulous Lending Is Taking Homes From the Poor

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By all appearances, the loan agreement Gloria Knight signed in 1995 was a classic transaction between savvy mortgage salesmen and an unsophisticated borrower in a poor Brooklyn neighborhood.

Ms. Knight, a retired teacher, says the salesmen who knocked on her door persuaded her to put her house up as collateral for an \$88,000 loan, at 13 percent interest, to help with bills and a previous loan — even though she had no income and no way to make the \$973 monthly payments.

But when she defaulted on her loan, leading to eviction notices last year, she ended up in the grip of something far larger than Delta Funding, a relatively obscure Long Island mortgage company that solicits business from poor homeowners. Delta's partner in trying to take her home is Bankers Trust Company, America's eighth-largest bank.

High-interest lending in poor neighborhoods has long produced high profits for lenders and, often, equally high burdens for homeowners. But the entry of big banks like Bankers Trust is part of a growing trend in such lending and has changed the equation. Over the last several years, Delta has converted hundreds of millions of dollars' worth of its mortgages into securities much like bonds, which it sells to investors through Bankers Trust.

In turn, Bankers Trust has provided Delta with hundreds of millions of investors' dollars, allowing it to make more loans and become a major player in high-interest lending in New York and 21 other states.

But there is a problem: a high percentage of the homeowners can't afford Delta's mortgages. Many say they were duped into taking the loans and now may lose their homes as Delta and Bankers Trust try to reclaim the money for their investors.

Delta and Bankers Trust defend their activities. But Delta's business

has recently produced civil lawsuits in three states, and advocates for the poor and social-services agencies say the company has generated more complaints of abusive lending than any other high-interest lender in New York City. They contend that Delta has taken advantage of scores of homeowners and violated Federal and state laws.

Ms. Knight, 55, who has since been found to be delusional by a psychiatrist for the city's Protective Services for Adults, cannot even afford electricity. She keeps warm with a kerosene heater and cooks over a makeshift grill in her backyard. But she had something that made her attractive to lenders like Delta: her row house in East New York, which was fully paid for and which served as security. Legal Services lawyers say she will now almost certainly lose it.

Last month, Chief Judge Charles P. Sifton of the Federal Court for the Eastern District of New York stopped the foreclosure sales of homes of three people who defaulted on Delta loans, because, he wrote, the mortgages "on their face" violated Federal law, and so the borrowers showed a good chance of winning their lawsuit.

The homeowners have sued Delta and Bankers Trust, claiming they violated, among other laws, a Federal prohibition on making loans based solely on equity in a house and not on a homeowner's ability to repay. The suit seeks to represent tens of thousands of other Delta borrowers who lawyers say are in similar circumstances.

Officials with Bankers Trust, which is being acquired by the German banking giant Deutsche Bank, declined repeated requests for interviews. On Friday, William McBride, a bank spokesman, said in a statement: "Bankers Trust's sole responsibility in these situations is to safeguard the interests of investors. We have no other connection to these actions."

Marc E. Miller, Delta's general counsel and a son of its founder, vigorously denied that the company engages in deceptive lending, saying it made no sense financially for the company to make loans it knew would fail. "There is sometimes this myth that's spread around that lenders do make money" from foreclosed properties, Mr. Miller said. "And it is a myth."

While refusing to comment on cases that are in litigation, he added that "if a loan simply doesn't make sense for a borrower, we won't do it."

But city real estate records show high foreclosure rates on Delta mortgages in some neighborhoods. In Brooklyn, where the company is most active in the city, a search of records found that 48 of 363 loans made by Delta in 1995 — or about 13 percent — have ended up in default, and Delta has begun foreclosure actions. For 1996 loans, the records show, the figure is 99 of 923 — more than 10 percent.

In its annual report to the Securities and Exchange Commission last year, Delta reported that 4.65 percent of all its loans were in foreclosure, calculated by the dollar amount of the loans.

According to Inside B&C Lending, an industry newsletter that reports statistics from several large lenders, about 2.65 percent of the high-risk loans nationwide, by dollar amount, were in foreclosure as of September 1998, the most recent date for which information was available. An additional 1.9 percent were 90 days delinquent and in danger of foreclosure.

Delta's critics contend that the company has devastated the lives of many working-class homeowners, most of them elderly. "These folks not only lose their homes, but lose every dime of equity they have built up, and in most cases this is all they have to show for years of hard work," said Josh Zinner, a lawyer with the Foreclosure Prevention Project for Seniors, a branch of South Brooklyn Legal Services set up last year to pursue claims of abusive lending.

Anna Dawson, a 67-year-old Brooklyn widow who is fighting Delta and Bankers Trust in state court for her home, may get help from prosecutors. The Brooklyn District Attorney's Office is investigating an independent broker who refers business to Delta and who, she contends, falsified her mortgage application without her knowledge to make it appear she could afford a \$99,000 mortgage with monthly payments of \$1,017.

In reality, her only income was roughly \$700 a month in survivor's benefits from her late husband. But her application included a letter saying she was an office manager at United Equities in Brooklyn and a lease that made it appear she rented out a floor of her home. The company does not exist at the address on the letter, and Ms. Dawson said she has not worked in more than two decades. She has no renter. In addition, the signature on the lease is not hers, she said.

Her loan became part of \$340 million worth of 1997 Delta mortgages put into a trust managed by Bankers Trust and sold to investors.

In a lawsuit filed in State Supreme Court in Brooklyn, her lawyers contend that the mortgage broker and a home-improvement contractor came to her house uninvited several times, persistently pushing her to get a loan for repairs to her house.

In the end, she was unable to make her payments, and Delta and Bankers Trust have begun to foreclose against her. Meanwhile, she said she was left with almost no proceeds of her loan — after paying Delta's fees, settling a previous low-interest loan and paying the same home-improvement contractor, who she said did little work.

The Growing Trade Of High-Risk Loans

High-interest lending became a big business in low-income neighborhoods nationwide after 1986, when a change in the Federal tax code gave a break to homeowners who took out second mortgages. But complaints about abuses began almost immediately. Unscrupulous finance companies often singled out homeowners, many of them elderly, who had substantial equity in their homes; in case of default, lenders could recoup the loan by taking the home.

In 1993, New York City's Department of Consumer Affairs reported that finance companies, usually working with crooked home-improvement contractors, had "fleeced thousands of lower-income and minority New York City homeowners" out of equity in their homes by tricking them into loans for repairs. The report added that the lenders often researched homeowners before approaching them, studying credit reports to determine whether they had paid off their first mortgage.

Many finance companies resold their mortgages to big banks. But Delta — founded in 1982 in by Sidney A. Miller, a former planner for insurance companies — was one of the first to see a vast untapped resource beyond the banks: the investment market. By converting loans into securities and selling them to investors, finance companies could generate a faster profit and have access to much more capital, and make many more loans.



Gloria Knight at her house in Brooklyn, which salesmen persuaded her to put up as collateral for an \$88,000 loan. She cooks outside because she has no gas or electricity.

Over the last decade, the market in asset-backed securities like those issued by Delta has grown from \$9 billion to more than \$140 billion, as investors pursued the rapidly expanding trade in high-risk auto loans, credit cards and home-equity loans. The size of the high-risk home-loan industry alone reached more than \$120 billion in loans issued nationwide in 1997, according to industry estimates.

Recently, big lenders like Chase Manhattan, Norwest, Nationsbank, General Electric, Keycorp, Countrywide Credit Industries and others have expanded their involvement in high-interest lending.

Delta began selling loans as securities in 1991, giving investors the right to share in mortgage interest payments, and Bankers Trust's California branch soon began to manage the trusts that held these securities. Delta's business zoomed. In 1994, it made about \$100 million in loans. By last year, according to its Federal securities filings, its loans increased to more than \$1 billion. It grew from about 150 employees to more than 1,000. In 1996, it went public, on the New York Stock Exchange, and in 1997 it reported profits of more than \$30 million.

William J. Brennan, a lawyer for the Atlanta Legal Aid Society who specializes in lending abuse cases and is familiar with lawsuits against Delta, criticizes Bankers Trust as Delta's "enablers."

"Bankers Trust would never make these kinds of loans themselves," he said, "but they put themselves in the position of enhancing the power of Delta Funding to engage in abusive lending. And they do it because there's lots of money to be made."

But in the view of Marc Miller, whose family runs Delta, based in Woodbury, N.Y., "there are many people who want and need a loan and can't get one. From that standpoint we fill a very legitimate niche in the consumer finance field."

An Incompetence Ruling, And Then Default

Gertrude Menzel, an elderly Queens woman who had lived in her two-story row house in Ridgewood since she was a teen-ager, took out an \$81,000 Delta mortgage in the summer of 1994, when she was 78. Five years later, Bankers Trust and Delta say Ms. Menzel owes more than \$123,000 in principal and interest, and they are trying to take her house.

There is no dispute that Ms. Menzel signed the loan papers. But little else is clear, including her motivation, since the first mortgage on the house was paid off and she appeared to have no debts. Her lawyer said that she was talked into the loan by an acquaintance who had previously taken financial advantage of her and ended up taking the proceeds of her loan for himself.

But questions remain about whether she was competent when she closed the mortgage in Delta's offices. Workers at a Queens center for the elderly, who saw her almost daily, said they noticed memory lapses and confused behavior well before the summer of 1994.

By Thanksgiving, six months after she got the mortgage, she "was wearing house slippers out into the cold and was not taking care of herself," said Thomas Crossman, who ran the Ridgewood Older Adult Center at the time.

In 1995, according to court papers, two psychiatrists hired by the center found symptoms of dementia and memory loss. One reported that she "does not have any knowledge of her assets or income."

By May 1995, Ms. Menzel was ruled legally incompetent in State Supreme Court, and she later defaulted on the mortgage.

But Bankers Trust argued in court papers that her mortgage was valid because Ms. Menzel had not been ruled incompetent before the closing. Partly for that reason, a State Supreme Court judge, Edwin Kassoff, declined to let Ms. Menzel out of the mortgage. Bankers Trust and Delta continue to fight her in court.

Delta's critics say that the company commonly works with aggressive, often unscrupulous mortgage brokers and home-improvement contractors who canvass poor neighborhoods, looking for elderly homeowners willing to put up their homes as collateral for loans to help with bills or home repairs.

A search of court records and Delta loan documents found that at least two people who have referred loans to Delta — John Gizze, the owner of a mortgage consulting firm in Hempstead, N.Y., and Gary Feldman, a Queens home-improvement contractor — have pleaded guilty to conspiracy to commit bank fraud in Federal court in cases unrelated to Delta. Both men admitted in court that they had falsified papers to exaggerate the income of borrowers.

Mr. Gizze's lawyer, Allen Drezin, said Mr. Gizze has subsequently had "some dealings with Delta Funding," but they "have been up to the standards of the industry." Mr. Feldman is now a defendant in a Federal civil suit filed by Mary Lewis, a Queens woman who claims he and Delta deceived her when she took out a home-equity mortgage in 1997.

In a telephone interview, Mr. Feldman said that he has closed few loans with Delta, and denied engaging in any deceptive lending practices in his dealings with the company.

Delta officials said they were unaware of the criminal past of either man, but they added that they do not routinely perform criminal background checks on brokers.

"Dealing with thousands of different brokers," said Mr. Miller, the general counsel, "it would, frankly, be impossible for us to stay on top of every broker at every instant."

The company is now the target of at least four Federal civil suits, three of which seek to represent classes of thousands of homeowners whom lawyers allege were deceived or mistreated by Delta.

The suit filed late last year in Federal District Court for the Eastern District, which includes Brooklyn and Queens, accuses Delta of consistently lending to people based on the equity of their homes and not on their ability to pay, a practice the plain-

tiffs' lawyers say has led to scores of foreclosures.

The suit also accuses Delta of breaking Federal law by charging exorbitant extra interest once a loan goes into default. (A review of Delta loan papers for several borrowers found that the interest commonly jumps to 24 percent after default. In New York, interest rates over 25 percent are prohibited by criminal usury laws.)

Delta and Bankers Trust, represented by a single law firm in the case, have not yet responded to the allegations in court.

In Mississippi and Georgia, two Federal civil suits allege that Delta is one of many high-interest mortgage lenders paying fees to mortgage brokers, which would violate Federal law. The suits allege that these fees are, in reality, a kickback to brokers for steering borrowers to the lenders, even though it may not be in the borrowers' best interest.

Delta officials deny the accusations. But in a similar Federal class-action case in New York, Delta recently settled with the plaintiffs in a confidential agreement, according to reports Delta filed with the Securities and Exchange Commission.

Mr. Miller said in a written statement that all such suits contain "accusations, rather than fact" and have been filed "solely for the purpose of delaying or preventing Delta Financial from protecting its rights."

Allegations of Deceit And Finder's Fees

But Delta has not always been successful in challenging claims of abuse. In November 1991, Theresa Leonardi went into the hospital with thyroid and heart problems, only a month after the death of her husband of 50 years. Three days after she was released from the hospital, according to a lawsuit she filed against Delta, she was taken to the lender's offices, then in Great Neck, N.Y., by a stockbroker who later pleaded guilty to mail fraud against her in a separate case and served time in prison.

Mrs. Leonardi took out a \$95,000 mortgage on her home in Sheepshead Bay, Brooklyn, but she said later in a lawsuit against Delta that she was never told she was signing loan papers and believed she was signing investment papers.

The papers described her as a 68-year-old self-employed investor making \$7,000 a month. In fact, she was almost 73 and was living mostly on Social Security.

In giving the loan to Mrs. Leonardi, according to court documents, Delta waived its written policy stating that income tax returns should be used to verify the income of loan applicants.

In the end, her lawyers say, all her mortgage proceeds went directly to the stockbroker, and Mrs. Leonardi never made a single loan payment. By December 1992, the bank began a foreclosure.

Carl Felsenfeld, a former Citicorp vice president who was an expert witness for Mrs. Leonardi, said in a deposition that the case showed "clear and convincing evidence of Delta's participation in the fraud perpetrated on Mrs. Leonardi."

Delta denied the accusations and pointed out that Mrs. Leonardi had chosen the unscrupulous stockbroker herself. "It is a sad commentary on our society," Marie Klasa, a Delta vice president, wrote in a letter in 1995, "that people must seek to blame others for their own errors in judgment."

But as the trial approached last summer, Delta agreed to pay Mrs. Leonardi \$200,000 — more than twice the amount of her mortgage — in a confidential settlement in which Delta admitted no wrongdoing.

Mr. Miller said the company settled because it believed it would be less costly than pursuing an appeal.

"The actual facts," he said, "are that Delta made a loan that made sense at the time to a woman who knew what she was doing at the time."

Mrs. Leonardi remembered it differently. "At no time did any of these people explain to me that I was signing papers for a mortgage on my home," she stated in court documents. "They merely pointed to the lines, and I signed or initialed as directed. At the time I was so weak that I couldn't walk without assistance and could not read any of the papers that I was asked to sign."